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What's inside

Editorial

We feature three articles in this edition.

The first article outlines the characteristics of a memorandum of understanding and a letter of intent, which are typically used to outline parties' intentions and lay foundations for entering into definitive agreements. The article explains the factors to be considered in assessing whether the documents are legally binding and sets out the advantages and disadvantages in using them.

The second article provides an overview of the Banking (Amendment) Ordinance 2025 enacted to build a mechanism to facilitate information sharing to combat financial crimes. Under the mechanism, authorized institutions such as banks may share with one another information of both corporate and individual accounts on a voluntary basis, when they become aware of any suspected prohibited conduct such as money laundering.

The third article outlines the main features of the Inland Revenue (Tax Deductions for Assisted Reproductive Service Expenses) Ordinance 2025, which introduces tax deduction for assisted reproductive service expenses under salaries tax and personal assessment to encourage childbirth and promote fertility in Hong Kong.

There are three case reports in this edition.

The first case discussed the proper construction of s.45 of the Stamp Duty Ordinance (Cap. 117), which exempts certain instruments from stamp duty in respect of the transfers of Hong Kong stock between "associated body corporates". In particular, it considered what types of "body corporate" would qualify for the exemption and the meaning of "issued share capital" under s.45 of Cap. 117.

In the second case, the Court of Appeal re-affirmed the established principle that a mortgagee-creditor owes no duty to the principal debtor to utilise a security, including exercising its power of sale over the mortgaged property, in good time.

The third case considered unfair prejudice petitions in respect of companies managed and controlled by family members. The Court of First Instance found that it is possible for a breach of trust to be so serious that the trust and confidence of a shareholder of the companies has been irreversibly breached, which necessitates a buy-out order.

Boyce Yung

Introduction

Memorandum of Understanding ("MOU") and Letter of Intent ("LOI") may serve to set out the basic understanding of the parties, frame complex transactions, clarify key deal points, identify obstacles and expedite decision making by the parties to a proposed transaction or project. Both MOU and LOI outline the parties' understandings and/or intentions and lay foundations for drafting and entering into definitive agreements. Generally speaking, LOI typically resembles a letter and may be used at an earlier stage in negotiations to express intent to negotiate and outline basic terms, while MOU typically resembles a contract and may be used at a later stage in negotiation to set out mutual intentions, cooperation and responsibilities. Having said that, both MOU and LOI are flexible in terms of format and structure and they can be varied greatly in form and substance depending on the intention of the parties.

This article will discuss the use of MOUs/LOIs in government context, the factors for determining whether an MOU or LOI is legally binding, as well as the advantages and disadvantages of an MOU or LOI.

Use of MOUs/LOIs in Government Context

The Government from time to time enters into MOUs or LOIs with outside parties such as public authorities of other jurisdictions, independent statutory bodies, international entities, trade associations or professional bodies. These MOUs or LOIs may be intended to facilitate regulatory cooperation or education exchanges, recognize overriding principles or set voluntary guidelines which are not binding but show goodwill in collaboration. They are commonly drafted to be non-binding on substantive terms (for instance, the commitment of the parties to achieve certain goals) but legally binding on procedural matters (for instance, confidentiality provisions obliging the parties to keep the information exchanged confidential).

Determining Factors on Enforceability

To determine whether an MOU or LOI (or any part of it) is legally enforceable, the following factors are relevant for consideration.

Language

The express wording in the MOU or LOI is the most important factor in determining the intent of the parties. Under Hong Kong law, if the parties do not intend the MOU or LOI or any part of its provisions to be binding, a clear statement to such effect should be included. To make such intention clear, some MOUs or LOIs include clauses such as "This MOU/LOI is non-binding …" or "the parties do not intend to be legally bound …".

A "subject to contract" provision rebuts the presumption of contractual intention. In *World Food Fair v Hong Kong Island Development*[1], it was held that the matters which had been agreed in the LOI concerned were always going to be subject to a formal lease being agreed between the parties since, inter alia, the LOI contained a standard clause stipulating that the terms were offered 'subject to formal lease'.

An MOU or LOI is not legally enforceable if it merely uses conditional language without definite commitment, including the words or terms like "intends", "will endeavour", "agrees in principle", or "mutually understands". Conversely, if an MOU or LOI is intended to be legally binding, the MOU or LOI would use more definite and certain terms which show clear intent to be legally accountable, including the words or terms like "agree", "is/are obligated" or "complies with"..

Performance

The partial or full performance of obligations in the MOU or LOI by one or both parties is also an important determining factor of the intention to be bound. The parties' actions after signing also determine enforceability. If both parties proceed to carry out the substantive obligations outlined in an MOU or LOI, this may indicate that they intended the agreement to have binding effect.

Title and Format

Title and format may be taken into account when assessing whether an MOU or LOI is legally binding. The title and format of an MOU or LOI can provide initial clues about the parties' intentions though they are not decisive in determining legal bindingness. The specific wording and clauses within the document carry greater weight.

[1] [2007] 1 HKC 387, (2006) 9 HKCFAR 735, [2007] 1 HKLRD 498 (CFA)

Negotiation Stage and Transaction Type

The stage of negotiation and the type of transaction are also relevant. Generally speaking, the more advanced the stage of negotiation at which the MOU or LOI is concluded, the greater likelihood of the binding effect of the MOU or LOI is. If the transaction is of a type which usually requires definitive agreements to formalize the deal, such as a sale and purchase of real properties, the MOU or LOI is less likely to be binding.

Advantages and disadvantages of MOU/LOI

Advantages

- Blueprint for Future Binding Agreements – The understanding reached between the parties after preliminary negotiation can be reduced into and formalized as an MOU or LOI. The document may then serve as a blueprint for future legally binding agreements, reducing uncertainties and disputes.

- Flexible and Cost Effective – Since the drafting of MOUs and LOIs is generally less time-consuming and expensive, parties can explore options more flexibly and quickly. Negotiations can then be streamlined, saving time and cost of the parties.

- Reduced Risk – For non-binding MOUs or LOIs, parties can walk away from the transaction without legal consequence if insurmountable obstacles to consummate the transaction are later identified. This reduces the risk of wasting time and costs in negotiating a detailed definitive agreement prematurely.

Disadvantages

- Lack of Enforceability – A non-binding MOU or LOI does not impose any obligations on the parties which are legally enforceable. A party has no legal recourse if the other party breaches the terms of a non-binding MOU or LOI. This may create uncertainties as one party may change its mind unilaterally and does not observe the terms of the MOU or LOI with no legal consequence.

- Potential for Misunderstanding – A poorly drafted MOU or LOI may create unintended outcomes for the parties (say a provision which is intended to be non-binding may unintendedly become binding due to misunderstanding or poor drafting), resulting in dispute or litigation.

- Potential for Wasted Time and Resources – In the case that an MOU or LOI is not legally binding, parties could freely withdraw without legal consequences. The time and resources for negotiating, drafting and executing the MOU or LOI will be wasted if either one party later changes his mind and withdraws.

Joyce Chan

Amendments to the Banking Ordinance (Cap. 155) – Information Sharing to Combat Financial Crimes

Introduction

The prevalent use of online banking and payment services has been exploited by criminals to move and conceal illicit funds in recent years. There has been a marked increase in fraud and money laundering, and victims often suffer from significant hardship and stress. At present, authorized institutions ("AIs") cannot alert one another the illicit activities owing to the contractual and common law confidentiality obligations and statutory data privacy requirements. This creates an information gap among AIs, and in turn a loophole to be exploited by criminals to rapidly move and conceal illicit funds through the banking system.

Against the above background, the Government introduced and gazetted the Banking (Amendment) Bill 2025 on 28 March 2025 to amend the Banking Ordinance (Cap. 155) ("BO") in order to build in a mechanism to facilitate information sharing among AIs and to fill the information gap ("Mechanism") for better detection and prevention of financial crimes. The Bill was passed by the Legislative Council on 4 June 2025 to become the Banking (Amendment) Ordinance 2025 ("Amendment Ordinance"). It will come into operation on a day to be appointed by the Secretary for Financial Services and the Treasury, expected to be within 2025.

The Amendment Ordinance provides a "safe harbour" for AIs to share with one another information of both corporate and individual accounts on a voluntary basis, when AIs become aware of any suspected prohibited conduct, i.e. money laundering, terrorist financing or financing of proliferation of weapons of mass destructions (collectively "Prohibited Conduct").

Key Features of the Mechanism

The Mechanism has the following key features:-

(a) Information sharing: The information to be disclosed under the Mechanism includes that related to an AI's customer and an entity, account or transaction associated with the said customer, which may be related to any Prohibited Conduct. Examples include bank account numbers, personal data, beneficial owners or connected parties, details of relevant transactions and reasons for suspicion of involvement of any Prohibited Conduct.

(b) Request and voluntary disclosure: Under the new section 68AAB of the BO, an AI ("requesting AI") may, under prescribed circumstances such as when it becomes aware that the customer's activities warrant inquiries by the AI to assess whether any Prohibited Conduct is involved, request another AI ("requested AI") to disclose information to assist the requesting AI in conducting an inquiry for detecting or preventing any Prohibited Conduct. In response to a request from the requesting AI, the requested AI may, under the new section 68AAC, disclose information to the requesting AI.

An AI may also disclose, on its own initiative (i.e. without receiving any request from a requesting AI), to another AI ("receiving AI") if it considers that the information may assist the receiving institution in detecting or preventing any Prohibited Conduct. The receiving AI may, on the same ground for assisting the detection or prevention of any Prohibited Conduct, further disclose the information received to another AI pursuant to the new section 68AAD.

The information may be disclosed on a bilateral or one-to-many basis through the Financial Intelligence Evaluation Sharing Tool launched in 2023 or other secure platforms ("designated platforms") to be designated by the Hong Kong Monetary Authority ("HKMA") under the new section 68AAM, without the need to obtain the consent of the entity to which the information is related, provided that the AI has reasonable grounds to believe that obtaining consent would risk prejudicing the AI's conduct of inquiries for detecting or preventing any Prohibited Conduct. Under new section 68AAH, HKMA may approve an AI to have access to the designated platform if HKMA is satisfied that the AI has adequate systems of control to ensure its compliance with the requirements under the Amendment Ordinance.

(c) "Safe harbour" protection: Under the new section 68AAG, the disclosure of information by AIs will not (i) be treated as a breach of any restriction on disclosure of information imposed by any contract, enactment, rule of conduct or other provisions; or (ii) render the AI that made the disclosure liable in damages for any loss arising out of the disclosure or any act or omission in consequence of the disclosure, provided that the AIs acted in good faith and with reasonable care in making the disclosure and complied with specified confidentiality requirement in the new section 68AAF(1).

Where an AI to which information is disclosed under the Mechanism (i) discloses the information as required or permitted by law or ordered by a court; or (ii) otherwise uses the information for detecting or preventing any Prohibited Conduct, such disclosure or use is not to be treated as a breach of obligation of confidence owed by the AIs.

The "safe harbour" aims to encourage voluntary and reasonable information sharing among AIs by offering legal protection to AIs, while striking an appropriate balance between detecting and preventing Prohibited Conduct and safeguarding data privacy and confidentiality. The HKMA will issue guidelines to facilitate AIs' compliance with the requirements under the Amendment Ordinance.

Implications

While there may be concerns regarding the possible increase in compliance costs, participation in the Mechanism will assist the AIs in mitigating the risks associated with fraud or any Prohibited Conduct, thereby protecting both AIs and their customers.

Moreover, the Mechanism will complement the existing suspicious transaction reporting ("STR") regime under the Organized and Serious Crimes Ordinance (Cap. 455) by enhancing the quality and the comprehensiveness of the information in STRs filed by AIs.

The Mechanism has personal data privacy implications in that it will allow AIs to share customers' information with other AIs and law enforcement agencies without obtaining the customers' consent. While permitting AIs to disclose and use information for the purpose of detecting or preventing Prohibited Conduct, the Amendment Ordinance prescribes conditions for such disclosure and imposes obligations on AIs to maintain confidentiality of the information disclosed and received. For example, AIs are required to act in good faith and with reasonable care, and information shall only be disclosed through secure channels. If an AI fails to comply with the specified conditions, it will lose the protection of the "safe harbour", including the protection against the liabilities under any enactment, such as the Personal Data (Privacy)

Ordinance (Cap. 486) or the common law.

Conclusion

The Amendment Ordinance intends to strike a balance between legitimate data privacy concerns and the need to protect customers of AIs from fraud and to minimize the risk of the banking system from being exploited by criminals. The Mechanism will enable AIs and law enforcement agencies of Hong Kong to take swift actions for early interception of illicit funds and to expedite intelligence gathering, which in turn will strengthen the protection of Hong Kong's banking system and enhance Hong Kong's status as an international financial centre. The public will also benefit from better protection against the Prohibited Conduct.

Connie Yip and Lawrence Li

Inland Revenue (Amendment) (Tax Deductions for Assisted Reproductive Service Expenses) Ordinance 2025

Introduction

As one of the Government's measures to promote fertility, the Inland Revenue (Amendment) (Tax Deductions for Assisted Reproductive Service Expenses) Ordinance 2025 ("Amendment Ordinance") was enacted in February 2025 to introduce a tax deduction for assisted reproductive ("AR") service expenses ("qualifying AR service expenses") under salaries tax and tax under personal assessment starting from the year of assessment 2024/25.

This article outlines the major features of the Amendment Ordinance.

Scope of qualifying AR service expenses

Under the Amendment Ordinance and the existing regulatory regime on AR services under the Human Reproductive Technology Ordinance (Cap. 561) ("HRTO"), the following two groups of persons receiving qualifying AR services for medical reasons are eligible for the tax deduction:

(a) infertile couples or persons under specified circumstances. The specified circumstances include (i) persons undergoing sex selection of embryos to avoid sex-linked genetic diseases under s.15(3) of the HRTO; and (ii) persons continuing to receive a reproductive technology ("RT") procedure who were parties to a marriage when gametes were, or an embryo was, placed in the body of a woman pursuant to the procedure under s.15(7) of the HRTO, who need not be parties to a marriage at the time of receiving the RT procedure; and

(b) cancer patients, or any other patients, who may be rendered infertile as a result of chemotherapy, radiotherapy, surgery or other medical treatment.

For the purposes of the Amendment Ordinance, "qualifying AR services" means:

(a) the provision of RT procedures as defined by s.2(1) of the HRTO (e.g. a medical, surgical or obstetric procedure assisting human reproduction by artificial means, such as in vitro fertilization, artificial insemination and the obtaining of gametes) pursuant to a specified licence ("RT licence", i.e. an artificial insemination by husband licence, a storage licence or a treatment licence issued by the Council on Human Reproductive Technology ("CHRT") as defined under s.2(1) of the Human Reproductive Technology (Licensing) Regulation (Cap. 561A)), including a medical service related to such RT procedure; or

(b) the handling, storing or disposing of gametes or an embryo (used or intended to be used in connection with an RT procedure) pursuant to an RT licence.

A medical service is related to an RT procedure if the medical service (including counselling service) is directly related to the RT procedure which is provided before, during or after the RT procedure is to be/is provided; and such medical service is provided, prescribed or referred by a registered medical practitioner (as defined under s.2(1) of the Medical Registration Ordinance (Cap. 161)) who holds any clinical responsibility for the recipient of the RT procedure. In this regard, generally speaking, medical services expenses paid which are directly related to the qualifying AR services including drug expenses, consultation fees, hormonal tests charges, laboratory fees, in-patient charges, and operation fees are tax deductible.

However, expenses paid for receiving RT procedures in an overseas institution are not tax deductible since RT procedures provided outside Hong Kong are not regulated by the HRTO. Expenses on gamete freezing services for non-medical reasons are also not tax deductible to avoid incentivizing the delay of childbearing plans.

Eligibility for deduction

A taxpayer will be eligible for tax deduction for qualifying AR service expenses paid by the taxpayer, the taxpayer's spouse (not living apart), or both of them. The qualifying AR services must be received by the taxpayer, the taxpayer's spouse, or both of them.

Claim of deduction by married persons

A married taxpayer may claim deduction for qualifying AR service expenses paid by the taxpayer or the taxpayer's spouse (not living apart), but expenses already claimed by the taxpayer's spouse should be excluded. The taxpayer and the taxpayer's spouse can decide how to allocate the amount of deduction claimed.

Maximum amount of deduction

The maximum amount of deduction allowable for a year of assessment is $100,000.

For married taxpayers, the maximum amount of deduction allowable for both the taxpayer and the taxpayer's spouse is $100,000 in total. Even if a taxpayer is married in more than one marriage during a year of assessment, the amount of deduction allowable to the taxpayer or the taxpayer's spouse or both of them shall not exceed $100,000.

Refund or reimbursement

Any refund or reimbursement (e.g. expenses reimbursed by insurance companies) shall be deducted from the qualifying AR service expenses paid. If the refund or reimbursement is made before a taxpayer claims the tax deduction, he/she can only claim the reduced amount of the qualifying AR service expenses paid. If the refund or reimbursement is made after a taxpayer claims the tax deduction, he/she must notify the Commissioner of Inland Revenue ("Commissioner") in writing of such refund or reimbursement within three months after the date of refund or reimbursement. If the tax deduction has been allowed, additional assessment may be made on the taxpayer having regard to the reduction.

If a taxpayer fails to notify the Commissioner in writing of the refund or reimbursement within the specified period without reasonable excuse, he/she commits an offence and is liable on conviction to a fine, as well as further fine in respect of the undercharged amount.

Standard form of proof

To claim for the tax deduction, the taxpayer should request a registered medical practitioner of a licensed centre who holds any clinical responsibility for the relevant RT procedure to sign and issue a standard form of proof for qualifying AR service expenses ("Proof") certifying the date and amount of qualifying AR service expenses paid, as well as the eligibility of the taxpayer for the tax deduction.[2] The taxpayer is not required to provide the Proof when filing the tax return; nevertheless, the Inland Revenue Department ("IRD") may request the taxpayer to submit the Proof as supporting evidence for the deduction claimed where necessary. Taxpayers should retain the Proof and relevant receipts for six years after the expiration of the relevant year of assessment for verification when required by the IRD.

Daisy Law

John Wiley & Sons UK2 LLP & Wiley International LLC v The Collector of Stamp Revenue [2025] HKCFA 11

This case concerns the proper construction of s.45 of the Stamp Duty Ordinance (Cap. 117) ("SDO"), which exempts certain instruments from stamp duty in respect of the transfers of Hong Kong stock between "associated body corporates" where one body corporate is the "beneficial owner of not less than 90 per cent of the issued share capital" of the other. The Court of Final Appeal ("CFA") considered two main questions:

(a) What types of "body corporate" qualify under s.45 of the SDO?
(b) What is the meaning of "issued share capital" under s.45 of the SDO?

Background

As part of an internal restructuring of the John Wiley & Sons group, John Wiley & Sons UK2 LLP ("Wiley LLP"), a UK-incorporated limited liability partnership ("LLP"), sold its entire shareholding in a Hong Kong subsidiary to Wiley International LLC ("HoldCo"), which indirectly owned Wiley LLP through an intermediary LLP.

Wiley LLP and HoldCo ("the Appellants") were assessed to *ad valorem* stamp duty in the amount of

[2] The standard form of the Proof is available on the CHRT's website at: https://www.chrt.org.hk/english/publications/files/form_of_proof.pdf

HK$6,361,204 for the transfer. They applied to the Collector of Stamp Revenue ("Collector") for exemption under s.45 of the SDO, which was denied on the basis that the Appellants were not "associated" with each other because Wiley LLP, as an LLP, did not have "issued share capital" that was at least 90% owned by HoldCo.

The Appellants successfully appealed against the Collector's assessment in the District Court.[3] The Court of Appeal ("CA") reversed the District Court's decision, holding that Wiley LLP did not have "share capital" so that the transfer fell outside the s.45 exemption.[4]

The Appellants further appealed to the CFA, arguing that Wiley LLP was a "body corporate" with "participation interests" analogous to "share capital" for the purpose of s.45 of the SDO, thus qualifying for the exemption.

CFA's decision

Types of "body corporate" qualify under s.45 of the SDO

The CFA traced the legislative history of s.45 of the SDO, noting that its predecessor (i.e. then s.5A) limited relief to transfers between "associated companies". The section was later renumbered as s.45 with the term "associated company" replaced with "associated body corporate".

At the time when the exemption under s.45 of the SDO was introduced, the old Companies Ordinance (Cap. 32) recognized three types of companies: companies limited by shares, companies limited by guarantee and unlimited companies. Among these, only companies limited by shares were required to have share capital. The other two types of companies could either have or not have a share capital.

In light of the foregoing, the CFA accepted that it was reasonable to infer that by extending the type of entities which may benefit the s.45 exemption from "associated companies" to "associated bodies corporate", the legislature intended to expand the scope of s.45 of the SDO from solely covering transfers between limited liability companies to encompassing transfers between all bodies corporate with share capital. This leads to the consideration of the next question – what is the meaning of "issued share capital" under s.45 of the SDO.

Meaning of "issued share capital"

An LLP is a relatively new business structure that emerged after the enactment of s.45 of the SDO. It is undisputed that an LLP cannot issue and allot share capital. In this regard, the Appellants contended that "issued share capital" in s.45 of the SDO should be interpreted to cover "a class of participation interest in the corpus and income of the corporation (or body corporate) issuing it that is economically and juristically analogous to share capital at Hong Kong law, albeit not necessarily identical to it". The Appellants further contended that by way of example, a "share" in the capital of an LLP is in proportion to the relevant capital contribution made by a member, and economic participation in the LLP is proportionate to the share of the member. However, these contentions of the Appellants were rejected by the CFA.

The CFA held that "issued share capital" under s.45 of the SDO should be interpreted in its ordinary and natural sense, consistent with its well-established meaning in company law. The CFA agreed with the CA that "issued share capital" in s.45 may be understood to mean "the total monetary value of the consideration paid (or given) or agreed to be paid (or given) by the shareholders in return for shares of a company as have been issued". The CFA emphasized that the phrase "issued share capital" should be read in the same way regardless of whether a foreign corporation was involved.

The CFA noted that the evidence in support of the leave application indicated that there were pending before the Collector a significant number of applications for relief on similar grounds to those presented by the present case. The CFA was of the view that whether s.45 of the SDO should be amended to address cases such as the present case is a matter for the legislature, not the court, to decide. In Singapore, by s.3 of the Stamp Duties (Amendment) Act 2008 (Act 36 of 2008), *ad valorem* relief was extended to LLPs, whether formed or incorporated in or outside Singapore. The absence of such relief in Hong Kong has given rise to the present litigation.

In light of the discussion above, the CFA unanimously dismissed the appeal.

Blondie Poon

[3] John Wiley & Sons UK2 LLP v Collector of Stamp Revenue [2022] 3 HKLRD 747.
[4] John Wiley & Sons UK2 LLP v Collector of Stamp Revenue [2024] 3 HKLRD 689.

Indian Overseas Bank v Seabulk Systems Inc [2024] HKCA 522

Facts

On 25 May 2007, the 1st Defendant ("D1") entered into a contract ("ZPMC Contract") with Zhenhua Port Machinery Co Ltd ("ZPMC") for the purchasing of one lot of bulk material handling equipment ("Equipment") to be integrated into and form part of a bulk material handling system at a port in Quebec, Canada.

Pursuant to the ZPMC Contract, D1 was to pay for the Equipment in instalments. As security for the performance of its obligations, ZPMC provided D1 with three advance payment guarantees and a performance guarantee (collectively "APGs") issued by the Bank of China, Shanghai branch ("BOC").

D1 financed the purchase of the Equipment by obtaining from the Plaintiff acting through its Hong Kong branch ("P") banking/credit facilities ("Facility").

D1's repayment obligations to P under the Facility were secured by, among others, D1's assignments of the APGs to P ("Assignment Agreements") and personal guarantees ("Guarantees") from the 2nd Defendant ("D2") and 3rd Defendant ("D3"), who were the directors and shareholders of D1. D1, D2 and D3 are collectively referred to as "Ds".

ZPMC delayed delivering the Equipment. On 30 April 2010, Ds requested P to invoke the APGs due to ZPMC's breach of its obligations under the ZPMC Contract. On 3 May 2010, P issued demand letters to BOC demanding for payments under the APGs. It was only after the APGs had expired on 7 May 2010 that BOC rejected P's demands.

On 11 May 2010, P asked BOC to enlighten them as to the "valid claiming documents required in order to invoke" the APGs. BOC replied that the Second Intermediate People's Court in Shanghai made four orders on 25 May 2010 restraining BOC from making payments under the APGs ("Restraint Orders"). The Restraint Orders subsequently led to a series of further proceedings in the People's Republic of China involving P, D1, BOC and ZPMC ("SH Proceedings").

CFI Proceedings

On 21 May 2012, P commenced proceedings against Ds in the Court of First Instance ("CFI") seeking for the repayment of the sums due under the Facility with interest and to enforce the Guarantees. Ds' defences to P's claim ("Defences") were mainly:

(i) P misrepresented its ability to competently handle the security;
(ii) P advised Ds in relation to the security and its advice was negligent; and
(iii) P owed each of Ds a duty to deal with the security in such a way as to maximize the value, and in breach of duty squandered the available security entirely; further or alternatively, P was negligent in dealing with the security.

The CFI judge ("Judge") rejected all the Defences and ruled in favour of P ("CFI Judgment").

The Appeal

D1 and D3 ("Appellants") appealed to the Court of Appeal ("CA") on the following grounds:

Ground 1: The value of the APGs was lost through P's act(s) and/or omission(s) arising from the breach of P's duties as lender. Being a lender in possession of security, P failed to properly utilize the APGs and the Assignment Agreements to reduce Ds' indebtedness;

Ground 2: The Judge erred in failing to hold that the operative cause of the loss of the APGs was P's conduct, including the failure to address and/or understand the correct claiming procedure, and its incompetent drafting of the claim documentation;

Ground 3: As the Judge disallowed P's application to amend its pleadings to raise the argument that D1 had consented/acquiesced to the way P prepared, handled and dealt with the Assignment Agreements and/or APGs, the Judge should not have allowed P to rely on the same acquiescence argument or made such findings in the CFI Judgment;

Ground 4: The Judge erred in law in upholding P's "suggestion" that D1 could itself have espoused a claim under the APGs;

Ground 5: The Judge was wrong to find that P's delay in making a demand under the APGs was caused entirely by Ds;

Ground 6: The Judge's comment that Ds' unwillingness and/or failure to assist P in the SH Proceedings ("Judge's Comment") implied that Ds' limited and belated participation in the SH Proceedings caused or contributed to the loss of the value of the APGs ("Value Loss Implication"), and the Judge's Comment was unsustainable; and

Ground 7: The Judge erred in holding that P was entitled to be indemnified by the Appellants jointly and severally in respect of all legal costs incurred as a result of the SH Proceedings.

CA affirmed the CFI Judgment and rejected each of the above Appellants' grounds of appeal based on the following:

Grounds (1) and (2)
The Appellants' proposition that P, as a mortgagee-creditor, was under a duty to utilize a security in good time was unsound in principle. The Judge correctly stated that a mortgagee-creditor owed no duty to the surety (or the principal debtor) to exercise its power of sale over the mortgaged securities and could decide in its own interest whether to sell and when to do so. The Assignment Agreements were valid but the right to make a demand under the security was not assigned to P and remained with D1. The Appellants' argument that P failed to properly understand the claiming procedure, or failed to make a claim in good time, was not valid on the facts found by the Judge. Even if P had the right to make a demand under the APGs or had D1 been the one who made a demand in time, it did not mean that BOC would have paid under the APGs.

Grounds (3) and (4)
The allegations under Grounds 3 and 4 were not sufficiently material to undermine the Judge's conclusion that P did not breach any of the alleged duties owed to Ds.

Ground (5)
There was no proper basis to interfere with the Judge's conclusions on the facts found by the Judge that P's delay in making a demand under the APGs was entirely caused by Ds. Even if Ds did not cause the delay, Ds failed to establish the complaint that P was in breach of duties owed to Ds.

Ground (6)
The Judge's Comment formed part of the factual matrix for reaching her conclusion that P had not done any act which was in breach of its duties or caused or contributed to the loss of the APGs' value. The Judge's Comment could not have given rise to the Value Loss Implication.

Ground (7)
The Judge did not err in holding that P was entitled to be indemnified by the Appellants in respect of all legal costs incurred as a result of the SH Proceeding because the indemnification clauses in the Assignment Agreements and the Guarantees entitled P to be indemnified.

Oswald Law

Harbour Front Ltd v Money Facts Ltd [2024] 3 HKLRD 299

Facts

The younger brother (through his corporate alter ego Harbour Front Ltd ("**HF**")) and the elder brother (collectively, "**Brothers**") used to manage and control two companies ("**Companies**"), namely, Money Facts Ltd ("**MF**") and Fonfair Co Ltd ("**Fonfair**"). A written shareholders' agreement was made between the Brothers. There was also an implicit agreement or understanding that the Brothers should participate equally in the conduct of the businesses of the Companies, and that neither was to be excluded from management and control unless for good reason such change should become necessary.

The younger brother was found to have misappropriated money from Fonfair, and disputes arose between the Brothers regarding the sale or development of the land held by Fonfair. The elder brother removed the younger brother from the boards of the Companies.

The younger brother, through HF, presented two series of unfair prejudice petitions in respect of the Companies in 2004 and 2018 and sought orders for participation in management of the Companies, but the petitions were dismissed by the Court. The present case concerned the third series of petitions by HF, which claimed that it had corrected the wrongs that it was found to have committed in the previous proceedings and was entitled to participate in the management of the Companies. The elder brother presented a cross-petition seeking a buy-out order of the shares in MF.

Analysis

The Court found that there was a "quasi-partnership" between the elder brother and HF in respect of their association in the Companies, giving rise to equitable considerations. The expression "quasi-partnership" means that a company has not just corporate personality and a constitution, but also scope for personal obligations and rights binding the shareholders in equity based on (i) a relationship of mutual trust and confidence, and (ii) an agreement or understanding that each shall have the right to participate in the management of the company. If the personal obligation and right, or the substratum of mutual trust and confidence, are deliberately or permanently renounced by a member, that member cannot expect that equity will allow him to hold the other members to their equitable obligations. The agreement or expectation of equal participation is not indefinite and is likely to be limited to a point in time at which for some other reason the change in management and control becomes necessary.

As to when it would become necessary for the agreement or expectation of equal participation to change, the Court looked at the Australian case *Nassar v Innovative Precasters Group Pty Ltd*[5], which held that in a "quasi-partnership" characterised by mutual cooperation and trust, the expectation of participation in the management would come to an end by reason of the emergence of irreconcilable differences whereby the relation between the shareholders became strained to the degree that they could not work together.

The line of authorities was traced back to *Ebrahimi v Westbourne Galleries*[6], where it was held that shareholders were not, by the mere fact of shareholding, entitled to participate in management.

In a similar vein, it was noted, as *obiter*, by the Court of Appeal in *Ng Yat Chi v Max Share Ltd (No. 2)*[7] that even if there was a special relationship between the parties, such a relationship would have come to an end when the petitioner destroyed the basis of the mutual trust and confidence by abusing his position and siphoning off the company's profits.

In relation to the key issue of what steps were adequate to remedy misconduct, the Court held that it would depend on the nature of the misconduct and the circumstances. The greater the seriousness of the misconduct, the number of instances, the period of time over which it had taken place, and the general behaviour of the recalcitrant shareholder were all material. It was obviously possible for breach of trust to be so serious that the trust and confidence of a shareholder had been irreversibly breached.

Disposition

The Court considered that, given the seriousness of the misconduct on the part of the younger brother and HF, it would not require much in order to demonstrate that trust and confidence had been permanently destroyed as a consequence of wrongdoings by HF that justified the Court finding unfair and prejudicial conduct and ordering a buy-out. Accordingly, HF's petitions failed and HF was ordered to purchase the elder brother's shares in MF.

Concluding Remarks

A company formed on the basis of a personal relationship involving mutual trust and confidence is often referred to as a "quasi-partnership" company. A shareholder excluded from management and control of the company due to his own wrongs must show a recognition of the seriousness of the misconduct and demonstrate a *bona fide* desire to restore the previous state of affairs in order to justify to the court that the other shareholder should act in accordance with their original understanding and agreement.

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5 [2009] NSWSC 342
6 [1973] AC 360, at 379B–G
7 [2001] 1 HKLRD 561